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SUBJECT: 2005-2006 INTERNATIONAL NARCOTICS CONTROL STRATEGY REPORT (INCSR) - ECUADOR - MONEY LAUNDERING SECTION

REF: STATE 210351

Ecuador's new comprehensive law against money laundering was published in the Official Register on October 18, 2005. The new law criminalizes the laundering of illicit funds from any source and penalizes the undeclared entry of more than $10,000 in cash. The law calls for the creation of a financial intelligence unit (FIU) under the purview of the Superintendency of Banks. Regulations for application of the law and establishment of the FIU have not yet been developed.

With a dollar economy and a geographical situation between two major drug producing countries, Ecuador is highly vulnerable to money laundering but is not considered an important regional financial center. Because there has been no effective control of money laundering until now, there is no way to judge confidently the magnitude of such activity in the country. In addition to concerns about illicit transactions through financial institutions, there are some indications that money laundering is taking place through "normal" commercial activity. Recurrent detections of large amounts of unexplained currency entering and leaving Ecuador indicate that transit and laundering of illicit cash are also significant activities. Though smuggled goods are regularly brought into the country, there is no evidence that they are significantly funded by drug proceeds.

A free trade zone law was passed in 1991 in order to promote exports, foreign investment and employment. The law provides for the import of raw materials and machinery free of duty and tax; the export of finished and semi-processed goods free of duty and tax; and tax exemptions for business activities in the government-established zones. Free trade zones have been established in Esmeraldas, Manabi and Pichincha provinces, and a new zone is planned for the site of the new Quito airport. There is no known evidence to indicate that the free trade zones are being used in trade-based money laundering.

The Narcotics and Psychotropic Substance Act of 1990 (Law 108) criminalized money laundering activities only in connection with illicit drug trafficking. Regulations issued pursuant to Law 108, the 1994 Financial System Law, and a 1996 Banking Superintendency Resolution require financial institutions to report to the National Drug Council (CONSEP) any transaction in cash or stocks over $5,000, as well as suspicious financial transactions. Mutual societies are required to report transactions of $5,000 and above. Financial cooperatives must report transactions of $2,000 and higher. Electronic reporting of this information was implemented in 1999. Banks operating in Ecuador are required to maintain financial transaction records for six years. There are no due diligence or banker negligence laws that hold individual bankers responsible if their institutions launder money. However, a bank's board of directors can be held legally responsible if drug money laundering occurs in their institution.

Some existing laws may conflict with the detection and prosecution of money laundering. For example, the Bank Secrecy Law severely limits the information that can be released by a financial institution directly to the police as part of any investigation, and the Banking Procedures Law reserves information on private bank accounts to the Banking Superintendency. In addition, the Criminal Defamation Law sanctions banks and other financial institutions that provide information about accounts to police or advise the police of suspicious transactions if no criminal activity is proven.

As a result of this contradictory legal framework, cooperation between other Government of Ecuador (GOE) agencies and the police has fallen short of the level needed for effective enforcement of money laundering statutes. Other problems conflicting with an anti-money laundering regime include the absence of regulations requiring financial institutions to exercise due diligence and the weak regulation of currency exchange businesses (casas de cambio).

As a result of these shortcomings, during the past five years there have been no serious investigations of drug money laundering in Ecuador. Without solid financial intelligence, it is impossible to estimate accurately the extent and nature of a money laundering problem in Ecuador. It is not known to what extent money laundering may be related to narcotics proceeds, or may be generated by other crimes such as contraband smuggling, illegal migration, corruption, bank fraud, or terrorism.

The need to develop regulations and establish agencies to implement the new money laundering law implies that it will be several months, at least, before effective action can be taken to

remedy this situation.
Several Ecuadorian banks maintain offshore offices. The Superintendency of Banks is responsible for oversight of both offshore and onshore financial institutions. Regulations are essentially the same for onshore and offshore banks, with the exception that offshore deposits no longer qualify for the government's deposit guarantee. Anonymous directors are not permitted. Licensing requirements are the same for offshore and onshore financial institutions. However, offshore banks are required to contract external auditors pre-qualified by the banking Superintendency. These private accounting firms perform the standard audits on offshore banks that would generally be undertaken by the Superintendency in Ecuador. Bearer shares are not permitted for banks or companies in Ecuador.
The Ministry of Foreign Affairs, Superintendency of Banks and the Association of Private Banks formed a working group in December 2004 to draft a law against terrorist financing. By year-end 2005, a draft law had been completed and sent to the Presidency for review. Pending promulgation of a new law, terrorist financing has not been criminalized in Ecuador. The Banking Superintendency has cooperated with the USG in requesting financial institutions to report transactions involving known terrorists, as designated by the United States as Specially Designated Global Terrorists pursuant to E.O. 13224 (on terrorist financing) or by the UN 1267 Sanctions Committee. No terrorist finance assets have been identified to date in Ecuador. The Superintendency would have to obtain a court order to freeze or seize such assets in the event they were identified in Ecuador. Ecuador has ratified (26 June 2004) the UN International Convention for the Suppression of the Financing of Terrorism. No steps have been taken to prevent the use of gold and precious metals to launder terrorist assets. Currently, there are no measures in place to prevent the misuse of charitable or non-profitable entities to finance terrorist activities.
Ecuador is a party to the 1988 UN Drug Convention and has ratified (September 17, 2002) the UN Convention against Transnational Organized Crime. Ecuador is a member of the OAS Inter-American Drug Abuse Control Commission (OAS/CICAD) Experts Group to Control Money Laundering. Ecuador is also a member of the South American Financial Action Task Force (GAFISUD). Ecuador and the United States have an Agreement for the Prevention and Control of Narcotic Related Money Laundering that entered into force in 1994 and an Agreement to Implement the United Nations Convention Against Illicit Trafficking in Narcotic Drugs and Psychotropic Substances of December 1988, as it relates to the transfer of confiscated property, securities and instrumentalities. There is also a Financial Information Exchange Agreement (FIEA) between the Government of Ecuador (GOE) and the U.S. to share information on currency transactions.
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